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June 6, 2011

Representative Wayne A. Schmidt, Chair
Representative Jon N. Switalski, Ranking Minority Member
House Commerce Committee
Lansing, Michigan 48933

Re: Senate Bill No. 12

Dear Representatives:

I have reviewed S.B. 12, a bill introduced by Senator Jansen which has passed the Senate and awaits consideration by the House of Representatives. I am not able to be present in Lansing at the Committee hearing set for June 7, but I am writing to advise you of my opposition to S.B. 12 and the reasons underlying this opposition.

S.B. 12 will make four changes in Michigan law: (1) prohibit the combining or consolidation of UI tax rates unless there has been a violation of Section 22(b)(1) or failure to conform to corporate formalities for an unlawful purpose, (2) allows the combination of rates where there has been a business transfer for the sole or primary purpose of reducing reimbursement rates or tax rates (called "contribution rates"), (3) prohibits consolidation or combination of UI tax accounts while administrative and court challenges remain pending, and (4) requires that employers would get attorney's fees and costs if the employer prevails in an appeal concerning combining or consolidation of UI tax rates.

S.B. 12 involves "SUTA dumping," a term that refers to actions by employers who try to avoid legitimate charges to their unemployment insurance (UI) employer tax accounts through business transfers and other business transformations that lower UI tax rates. In order to understand S.B. 12, some technical background must be explained.

In 2004, Congress passed the "SUTA Dumping Prevention Act." This law required (among other changes) that states mandate experience rated UI rates be transferred in some cases while it prohibited transfers of UI experience rates in certain other cases. Since passage of this federal law, Michigan has been trying without success to properly and fully implement this federal conformity requirement.

As noted, the SUTA Dumping Prevention Act requires that states' UI laws include two tax provisions; first, a requirement that mandates a transfer of unemployment experience tax rates whenever there is substantially common ownership, management, or control of two employers; and, second, a prohibition on tax transfers between two business entities whenever an person acquires a business "solely or primarily" for the purpose of obtaining a lower UI tax rate.

Currently, Michigan law does NOT clearly conform to the mandatory rate transfer requirement of federal law because Section 22(b)(1)(a) of the MES Act limits mandatory transfers of UI experience tax rates to cases in which the "sole or primary" purpose of the business transaction in question was for the purpose of obtaining a lower UI tax rate. The "sole or primary" limitation is supposed to pertain only to those tax transfers that are prohibited under SUTA dumping. Michigan's law applies the "sole or primary" limitation to both the mandated transfer of tax rates and the prohibited transfers of tax rates. Michigan has been notified of this federal conformity issue by U.S. Department of Labor on three or four occasions since 2006. Sadly, S.B. 12 does NOT remedy this gap in Michigan's SUTA dumping law and will not bring Michigan law into conformity with federal law in relation to mandatory transfers of experience rating whenever two businesses operate under common ownership, management, or control.

Because S.B. 12 does not address the conformity of SUTA dumping in Michigan, it should not be considered a "conformity bill." Instead, S.B. 12 makes changes in Michigan law that will make it more difficult to address SUTA dumping while creating other potential issues in implementing federal and Michigan SUTA dumping law.

First of all, S.B. 12 adds a new subsection, numbered Section 22c(1), that will impose added limits on combination or consolidation of UI tax accounts unless the agency can establish a violation of existing Section 22b(1) or a disregard of separate legal entities' corporate formalities. There is no obvious rationale for these changes, other than offering added technical language to Michigan's SUTA dumping rules and creating a potential for confusion and misunderstanding on the part of reviewing courts.

Second, S.B. 12 proposes in subsection 22c(2) that combination or consolidation of employer UI tax accounts is delayed until all administrative and judicial appeals are final. This provision would make UI tax cases effective only when a final appeal is resolved. This is in contrast to benefit payments and tax credits to employer experience accounts, both of which happen immediately and are adjusted upon completion of appeals. So, for example, if a redetermination is issued that reverses an earlier determination awarding UI benefits, UI benefits are stopped, the employer's account is credited, and an overpayment of benefits is created. In other words, agency decisions awarding or denying benefits are immediately effective, as are the related employer tax charging and credit mechanisms.

The rationale for treating UI tax cases in a different manner than all other UI adjudications is not immediately evident. Indeed, U.S. Department of Labor guidance states that "the Department strongly recommends that states reassign rates immediately upon completion of the [business] transfer" or "the next time the state calculates rates for all employers." Currently, UI appeals can take up to 3 years to resolve if an appeal to the Court of Appeals is pursued, and possibly longer if review is sought in the Supreme Court. For this reason, the delay provision creates a strong incentive for employers to litigate UI tax cases largely to gain a delay in imposition of higher tax rates without sufficient regard for the merits of appeals. Accordingly, we would not support this change in law.

Third, subsection 22c, as proposed by S.B. 12, would add a final provision that would permit employers who prevail in tax case appeals to get court costs and attorney's fees assessed against the state agency. This provision might seem appealing upon first glance, but it violates current practice in a number of ways. First, costs are rarely assessed in appeals under the MES Act as with most forms of civil litigation in Michigan. This policy was expressed in early court cases which found that a "public question" was concerned when denying costs in all cases interpreting the MES Act. Indeed, Section 31 of the Act prohibits charging UI claimants with costs or fees before the agency or the courts. Second, the bill proposes a one-sided costs option in which employers would not be required to pay costs even if they pursued frivolous appeals simply to delay tax cases. If we are going to start assessing costs in UI appeals, a more balanced approach would make both sides of a UI appeal equally exposed to imposition of costs and fees. In my view, rather than assessing costs against any party, it would be better to continue current policy and not bring costs and attorney's fees into UI appeals.

Thank you for this opportunity to express my views on this legislation. If you need further information regarding this matter, do not hesitate to contact me.

Sincerely yours,

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